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No. 87-963

IN THE
Supreme Court of the United States
OCTOBER TERM, 1987

ROBERT L. HERNANDEZ,
Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the First Circuit

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REPLY BRIEF FOR PETITIONER

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REPLY BRIEF FOR PETITIONER

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1. In its brief in response to petitioner's request for certiorari, the government agrees with petitioner that the decision of the court below, along with two other courts of appeals decisions, *Graham v. Commissioner*, 822 F.2d 844 (9th Cir. 1987) and *Miller v. Internal Revenue Service*, 829 F.2d 500 (4th Cir. 1987), *petition for cert. filed*, March 1, 1988 (No. 87-1449), "conflicts with the decision of the Eighth Circuit in *Staples v. Commissioner*, 821 F.2d 1324 (8th Cir. 1987)," *petition for cert. filed*, February 19, 1988 (No. 87-1382). Br. Resp. at 6.

In addition, as in its own petition in *Staples*, the government observes that if the "conflicting holdings" among the courts of appeals in these related cases are permitted to stand "disparate tax treatment for similarly situated

taxpayers" will result. Br. Resp. at 7. The government also emphasizes the important conflicts in the decisions in the courts of appeals on the "validity of the legal proposition" at issue here and in particular, over the applicability to religious services of this Court's holding in *United States v. American Bar Endowment*, 477 U.S. 105 (1986), which denied charitable contribution deductions for payments to purchase life insurance. *Id.* at 7. Accordingly, the government does "not oppose the petition" in this case with respect to "the statutory question presented" [1] *Id.* at 6. The government suggests, however, that there is "no reason" for this Court to review the constitutional issues presented (*Id.* at 9), and that it "would be preferable" for this Court to address the issues presented here in the Ninth Circuit case *Graham*

[1] Contrary to the impression that the government attempts to create in its brief (Br. Resp. 3-4), there is no issue in this case concerning the appropriateness of the behavior or operations of the churches and missions that received the payments at issue here. The parties stipulated that Scientology, the faith whose sacraments are at issue here is a religion (Pet. App. 32a, ¶ 52) and that the recipients of the contributions, the relevant Scientology missions and churches, were, at all relevant times, churches within the meaning of Internal Revenue Code § 170(b)(1)(A)(i) and tax-exempt religious organizations under § 501(c)(3) of the Code eligible to receive contributions deductible under § 170 (Pet. App. 32a, ¶ 53).

These stipulations mean that, as a § 501(c)(3) organization, each Scientology church that received the donations at issue here "engages primarily in activities which accomplish one or more of [the] exempt purposes specified in Section 501(c)(3), [and no] more than an insubstantial part of its activities is not in furtherance of an exempt purpose." Treas. Reg. § 501(c)(3)-1(c)(1). The stipulations indicate that the exempt charitable purpose of Scientology is the "advancement of religion." Treas. Reg. 1.501(c)(3)-1(d)(2). Thus, the stipulations here contradict the government's recitation of factual findings of the Tax Court in a completely separate case that one church of this religion was not eligible for tax exemption in the years 1970-1972. *See Church of Scientology of California v. Commissioner*, 83 T.C. 382 (1984), *aff'd*, 823 F.2d 1310 (9th Cir. 1987); Br. Resp. at 4, n.5. The government's recitation regarding that case is, at best, irrelevant.

v. Commissioner, 822 F.2d 844 (9th Cir. 1987), rather than in this First Circuit case. (*Id.* at 8). Each of these contentions of the government will be addressed in turn.

2. A decision in favor of the government on the statutory issues involved in this case necessarily raises substantial constitutional questions under the first amendment. In *Staples*, the court, by reversing the Tax Court's decision and holding that the receipt of religious services cannot constitute the kind of "material, financial or economic benefit" receipt of which may make payments nondeductible under § 170, did not need to reach the constitutional question. In the decision below, however, as well as in *Miller* and in *Graham*, the courts, in holding that § 170 of the Internal Revenue Code required disallowance of the deductions at issue, also necessarily addressed the taxpayers' contentions that the Commissioner's application of § 170 of the Internal Revenue Code violates the religion clauses of the first amendment.

In now claiming that this Court should deny review of the constitutional issues raised by the decision below, the government ignores important constitutional claims raised by petitioner under both the establishment and the free exercise clauses of the first amendment. First, the government erroneously characterizes petitioner's constitutional claim as limited to the issue whether denial of the charitable deduction in this case involves an unconstitutional "denominational preference." In addition, in its effort to depict as unimportant the petitioner's contentions regarding the establishment of a constitutionally prohibited denominational preference, the government treats the very issue of statutory interpretation that is in controversy here as if it had already been decided in the government's favor.[2] Br. Resp. at 8-9. By so doing,

[2] An additional claim by the government that the constitutional issue is unimportant seems to be contained in its assertion that the treatment of the constitutional matters in the taxpayer's petition was "briefly argue[d]." Br. Resp. at 8, *citing* Pet. 25-27. The

the government itself demonstrates that the issues of statutory construction and constitutional interpretation in this case are inextricably intertwined and must both be considered for petitioner to be accorded a fair hearing on the substantive merits of his case.

In claiming that its proposed application of section 170 of the Internal Revenue Code is neutral across all religious denominations, the government simply asserts that the payments made by the petitioner here solely to participate in the core religious sacraments of his church do not fall within the Revenue Rulings that allow—without any question as to the nature or value of the religious services involved—deductions under section 170 for "pew rents, assessments, church dues *and the like*." Br. Resp. at 9, *citing* A.R.M. 2, 1 C.B. 150 (1919), *reprinted in* Pet. App. 57a (*updated and reaffirmed* in Revenue Ruling 70-47, 1970-1 C.B. 49) (emphasis added). The applicability of that Revenue Ruling and its underlying policy of distinguishing religious from secular services under § 170, of course, is the very issue in this case. *See* Pet. at 10-24. The Eighth Circuit in *Staples*, 821 F.2d at 1327, explicitly analogized the payments at issue here to the "passing of the collection plate in church," and found no important difference between the payments in this case and those payments for participation in religious services addressed in the prior Revenue Rulings. 821 F.2d at 1326-28. The contention in the government's brief that there

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government's point here seems rather silly, but in making it, the government overlooks entirely taxpayer's arguments (Pet. at 21-24) that application of the legal standard established by this Court in a case involving payments for insurance policies, *United States v. American Bar Endowment*, 477 U.S. 105, to the religious services at issue here would violate first amendment prohibitions on entanglement of church and state by requiring IRS valuation of religious services. Moreover, if, as the government seems to suggest, page counting is a method of assessing an issue's importance, it is worth noting that two-thirds of the opinion below (Pet. App. 9a-28a) was devoted to analysis of the constitutional issues.

is no substantial constitutional issue in this case, therefore, is based entirely on its assumption of the validity of its interpretation of the very statutory question that is at issue here.

The peculiar interpretation advanced in the government's Brief in Response that the Commissioner's rulings regarding analogous payments to other churches and synagogues have no application to this case was explicitly rejected not only by the Eighth Circuit but also by the court below and the other two appellate courts that have agreed that the payments at issue here are not deductible. *See Hernandez v. Commissioner*, 819 F.2d 1212, 1227, Pet. App. at 27a ("[W]e have some doubt as to the continuing validity of the presumption in Rev. Rul. 70-47, 170-1 C.B. 39 [sic], that pew rents and mandatory church dues are tax deductible gifts. . . ."); *Graham v. Commissioner*, 822 F.2d 844, 850 (9th Cir. 1987) ("We are not convinced that . . . those rulings would comport with the analysis of section 170 that we have set forth here."); *Miller v. Internal Revenue Service*, 829 F.2d 500, 505 (4th Cir. 1987) ("We have no reason to believe that the IRS will fail to apply the principles that *emerge from this litigation* in its treatment of other religious groups.") (emphasis added.) Indeed, the series of suggestions advanced by the government both in its Brief in Response here and in its briefs below that all other payments to participate in religious services by adherents of all other religious faiths would remain deductible under § 170 make clear that the government is urging an application of § 170 by which it intends to deny charitable deductions for participation in religious services only by members of the Scientology faith. Such a policy creates an unconstitutional denominational preference under the establishment clause of the first amendment. *See Larson v. Valente*, 456 U.S. 228, 244 (1982).

In addition to the constitutional issue raised by the denominational preference that would be created by the

government's interpretation of § 170, other important first amendment issues that merit review by this Court are raised by the interpretation of § 170 adopted by the court below. As the government's Brief in Response indicates, the court below applied to payments solely for religious services, the legal standard adopted by this court in *United States v. American Bar Endowment*, 477 U.S. 105, a case denying charitable deductions for taxpayers' payments to purchase insurance: "The taxpayer, therefore, must at a minimum demonstrate that he contributed money or property *in excess of the value of any benefit he received in return.*" 477 U.S. at 118, *quoted in* Br. Resp. at 5 (emphasis added). Where a payment is made and, in return, religious services are received, important first amendment issues are raised that simply are not at stake when this legal standard is applied—as it always has been prior to this litigation—only to secular services such as insurance. Therefore, the fundamental issue of statutory interpretation at issue here—whether to apply the legal standard announced in the *American Bar Endowment* case to payments in exchange solely for participation in religious sacraments—cannot be separated from the special treatment of religion under the first amendment. Even the court below recognized that important "constitutional difficulties" may arise where the valuation of religious sacraments is at issue. *Hernandez v. Commissioner*, 819 F.2d at 1218. The Eighth Circuit in *Staples* remarked upon the "incongruity of attempting to place a market value on religious participation" and concluded that "[s]piritual gain to an individual church member cannot be valued by any measure known in the secular realm." 821 F.2d at 1327.

Indeed, special concern for entanglement with churches seems to account for the sharp distinction in IRS policy, heretofore consistently followed, between allowing without question deductions for membership dues to churches and synagogues and reducing deductions for membership dues to secular organizations by the value of secular

benefits made available to members. *Compare* Rev. Rul. 70-47, 1970-1 C.B. 49 (*reaffirming* A.R.M. 2, 1 C.B. 150 (1919)) (allowing deduction for all membership dues paid to churches and synagogues without inquiring into the value of such church memberships) *with* Rev. Rul. 68-432, 1968-1 C.B. 104 (detailing various instances where membership dues to secular charities are deductible only in part because the deduction is reduced by the value of secular benefits made available to members). Congress' special consideration of religion and churches throughout the Internal Revenue Code is a response to first amendment concerns. *See, e.g.*, 26 U.S.C. § 7611 (relating to restrictions on church tax inquiries and examinations); § 6033(a)(2)(A)(i) (exemption for churches from annual information return filing requirements).

As the taxpayer's Petition in this case details, at least two of the three methods offered by the court below for valuing the religious services which are at issue here violate the establishment clause of the first amendment. Pet. at 22-24.[3] The very notion of comparing relative values of religious services or determining allowable charitable deductions based on the costs to a church of providing religious sacraments is repugnant to the first amendment's prohibitions on entanglement of church and state both because it requires the valuation of religious services and creates denominational preferences. *See Walz v. Tax Commissioner*, 397 U.S. 664, 674 (1970); *Larson v. Valente*, 456 U.S. 228, 234 (1982).

In addition, the courts that have affirmed the Tax Court's decision, including the court below, have misapplied this Court's holdings regarding the protections of the first amendment in *Bob Jones University v. United States*, 461 U.S. 574, 603-04 (1983) and in *United States v. Lee*, 455 U.S. 252 (1982). The Tax Court found

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[3] The third method is contrary to IRS rulings and case law interpreting § 170. *See* Pet. at 23.

that the method used by the Church of Scientology of raising funds from its members was its method of implementing a sincerely held religious belief, the Doctrine of Exchange. Pet. App. 33a-34a. *See also* Pet. at 8 n. 4. The affirming courts of appeals have failed to recognize that the disallowance of a tax deduction for payments solely to participate in religious sacraments imposes a burden on taxpayers' religious practices by subjecting them to income tax, which burden requires the government to demonstrate both that a compelling state interest exists for its actions and that no less restrictive alternative is available. *Bob Jones University v. United States*, 461 U.S. at 603-04.

Moreover, the three affirming courts of appeals have accepted without question the IRS' claim that a compelling state interest exists here in the need to maintain a sound and uniform tax system. Although the *Lee* case, 455 U.S. 252, establishes that the need for a sound and uniform tax system can satisfy the government's burden of showing a compelling state interest, that case does not give the government a license simply to assert that any interpretation of the tax law automatically satisfies its constitutional burden. Indeed, the interpretation of § 170 being advanced by the government in this case represents a move from uniform tax administration among religions to an unpredictable, discretionary and non-uniform tax system. The IRS practice—consistently followed from the publication of A.R.M. 2, 1 C.B. 150, in 1919 until the inception of this litigation—of allowing charitable deductions for payments for religious services, regardless of their *form* or *nature* or *value*, has provided sound tax administration for seven decades. There is no compelling state interest for the rule being advanced by the government here.

3. In its brief in the instant case, the government indicates that "if possible," it "would be preferable for

this Court to consider the question presented here" in the *Graham* case, and has indicated that it does "not intend to oppose" the taxpayer's petition in that case. Br. Resp. at 8. The government asserts that in *Graham*, "a concrete factual context" exists. *Id.* The basis for the government's preference for the *Graham* case is mysterious. Since the entirety of the record in *Graham* was stipulated to be part of the record in the instant case, as well as to be included in the record in the *Staples*, and *Miller* cases, there is nothing in the *Graham* record that was not before the courts of appeals in these other cases and nothing that would not be before this Court if it grants review in any of these cases. Moreover, a case and controversy is equally present between the taxpayers and the government in each of these cases and each case raises identical legal issues.

There are a variety of alternatives that the Court might pursue in reviewing one or more of these related cases. For example, the Court could grant review in each of the related cases and consolidate them for argument; since counsel in this case represents all the taxpayers in each of these cases, such consolidation would not require any additional time for argument or briefing by the taxpayers or the government. Alternatively, the Court may wish to grant the taxpayer's petitions in this case, the first case before the Court, and hold the petition in the related cases pending its disposition. With three petitions having been filed, both by taxpayers and by the government, there seems little reason to delay resolution of these important issues in the present case while awaiting the filing of a fourth petition based upon the identical Tax Court record.

CONCLUSION

The pending petition for a writ of certiorari in this case should be disposed of as appropriate in light of the pending petitions of certiorari in *Commissioner v. Staples*, No. 87-1382 and in *Miller v. Commissioner*, No. 87-1449.

Respectfully submitted,

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